

● IFRS 17 EXPLAINED · EPISODE 5

PREMIUM ALLOCATION APPROACH (PAA)

The simplified model for short-duration contracts

IFRS 17

PSAK 117

OJK

PAA

GMM

PARA 53–59

IFRS 17 · Para 53

Para 54 · Para 55

Para 56 · Para 57

Para 58 · Para 59

PSAK 117 · OJK

IAI · 2025

LRC · GMM · PAA

The Premium Allocation Approach

A simplified model for short-duration contracts



WHAT IS THE PAA?

A simplified alternative to the **GMM/BBA** under IFRS 17 Para 53–59 — designed for short-duration contracts where GMM complexity adds little informational value.



LRC — SIMPLIFIED TO UPR

The **Liability for Remaining Coverage** is calculated similarly to the traditional Unearned Premium Reserve — no CSM measurement or tracking required.



LIC — STILL FOLLOWS GMM

PAA does **not** simplify the **Liability for Incurred Claims** — that still follows full GMM principles including IBNR and claims development.



WHO BENEFITS?

P&C insurers with motor, property, travel, and annual health contracts — reducing actuarial complexity and implementation cost significantly.



A huge benefit of the PAA is that general insurers will not be required to estimate future claims or do any form of CSM measurement or tracking.

— GRANT THORNTON, 2021

PAA Eligibility: Two Pathways

PATHWAY 1 — AUTOMATIC



Coverage $\leq$ 1 Year

Para 53(a)

 **No further testing required.** If every contract in the group has a coverage period of one year or less, PAA eligibility is automatic at initial recognition.

 **Motor insurance** — annual policies, third-party liability, comprehensive cover

 **Property & travel insurance** — fire, marine cargo, short-term travel policies

 **Annual health & group life** — annually renewable contracts, PA insurance

 **Most P&C insurers qualify automatically** — the PAA mirrors the traditional UPR method already in use

OR

PATHWAY 2 — DEMONSTRATED



Coverage $>$ 1 Year

Para 53(b)

 **Materiality test required.** The entity must reasonably expect that PAA measurement would not differ materially from GMM throughout the coverage period.

 **Run both models:** Calculate LRC under PAA and GMM, then compare the difference — Grant Thornton (2021) notes many firms must run GMM anyway to demonstrate eligibility.

 **ITB 2025 threshold:** LRC difference $<$ 15% → PAA eligible. LRC difference $\geq$ 15% → GMM required. No reassessment after initial recognition.

 **Tested once at initial recognition** — eligibility is NOT reassessed in subsequent reporting periods once determined.

 **Key risk:** If PAA $\approx$ GMM cannot be demonstrated, the entity must apply the full GMM — including CSM tracking — for that group

LRC Under PAA: The Simplified Calculation

IFRS 17 PARA 55–56

PAA CORE FORMULA

“ **LRC = Premiums Received – Acquisition Costs** ”

the PAA's elegant simplification of the GMM.

Revenue recognised on a straight-line basis (passage of time) or following the expected pattern of risk — Grant Thornton (2021) & IFRS 17 Para 56



No PVFCF

NO PRESENT VALUE

No discounting of future cash flows required for LRC



No RA

NO RISK ADJUSTMENT

Risk adjustment not required for LRC under PAA



No CSM

NO CSM TRACKING

Contractual service margin not tracked for LRC



No Disc.

NO DISCOUNTING

Unless financing component exceeds 12 months (Para 56b)

 Essentially the traditional **Unearned Premium Reserve (UPR)** approach, now formalised under IFRS 17 & PSAK 117

LRC Roll-Forward: PAA vs GMM Side-by-Side

ANNUAL PREMIUM **RP 1,200,000**

ACQUISITION COST **RP 120,000 (10%)**

COVERAGE **12 MONTHS**

PRODUCT **MOTOR INSURANCE**



INCEPTION LRC (Q0)

Rp **1,080,000**

Premium Rp 1.2M – Acq. Cost Rp 120K

Q1 LRC BALANCE

Rp **810,000**

3 months revenue recognised @ Rp 90K/mo

Q2 LRC BALANCE

Rp **540,000**

6 months revenue recognised

Q3 LRC BALANCE

Rp **270,000**

9 months revenue recognised

Q4 LRC BALANCE

Rp **0**

Full coverage period elapsed

✓ **KEY FINDING**

PAA ≈ GMM for 1-year motor → PAA eligible (diff <15%)

PAA Premium – Acq. Cost, straight-line release. No PVFCF, no CSM.

GMM PVFCF + Risk Adj. + CSM tracking every period.

LIC Under PAA: No Simplification Here



LIC Formula — Same as GMM

The PAA **does not simplify the LIC**. It is measured using the same GMM principles: **current FCF estimates** (best estimate of claims + expenses) **plus risk adjustment** for non-financial risk — always required, no exceptions.

FCF ESTIMATES

RISK ADJUSTMENT

PARA 59



Discounting Trigger — The 1-Year Rule

Discounting of LIC is **required** when cash flows are expected to be settled **more than one year** after the incurred claim date. The discount rate applied is the rate **at the date of the incurred claim** — locked in at that point.

>12 MONTHS → DISCOUNT

PARA 59(B)



Short-Tail P&C — Usually No Discounting

Motor insurance and property claims typically settle **within 12 months** of the claim date. As a result, discounting of LIC is **generally not required** for these lines — a practical relief for most Indonesian general insurers.

MOTOR

PROPERTY

≤12 MONTHS



Long-Tail P&C — Discounting Required

Liability, workers' compensation, and marine lines may have settlements extending **beyond 12 months**. Discounting is **required** — adding actuarial complexity similar to GMM. CIA/CAS (2023) confirms P&C discounting is primarily relevant for these long-tail lines.

LIABILITY

WORKERS' COMP

MARINE

Onerous Contracts Under PAA

IFRS 17 · PARA 57

“ If **FCF** > **LRC carrying amount** → Contract is **Onerous** →
Loss Component recognised in **P&L immediately** ”

IFRS 17 Para 57 — Simplified Onerous Test under Premium Allocation Approach



Para 57

ONEROUS TEST RULE

FCF vs LRC carrying amount — simplified approach under PAA at initial recognition



Assume NOT

IASB PRESUMPTION

Assume contracts are not onerous unless facts & circumstances indicate otherwise



CR > 100%

ONEROUS INDICATOR

$(\text{Claims} + \text{Expenses}) \div \text{Earned Premium} > 100\%$ signals potential onerousness



Same as GMM

LC TRACKING RULES

Loss Component sits within LRC; reverses before CSM rebuilds; tested every reporting date

i Key Insight: Despite PAA's simplicity, onerous contract testing is mandatory — Loss Component rules (Para 47–52) apply identically to both PAA and GMM.

PAA vs GMM — What's Simplified, What's Not

IFRS 17 · PSAK 117 — MEASUREMENT MODEL COMPARISON ACROSS 9 KEY DIMENSIONS

DIMENSION	🟢 PAA — PREMIUM ALLOCATION APPROACH	📊 GMM — GENERAL MEASUREMENT MODEL
📊 LRC MEASUREMENT	Premium-based (UPR-like) SIMPLE · Para 55	PVFCF + Risk Adjustment + CSM COMPLEX · Para 32
📈 CSM TRACKING	Not required SIMPLIFIED · No CSM calculated	Mandatory every reporting period MANDATORY · Para 44
📅 REVENUE RECOGNITION	Passage of time or risk pattern FLEXIBLE · Para 55(b)	Coverage units allocation ACTUARIAL · Para 44(e)
📉 LRC DISCOUNTING	Not required unless significant financing OFTEN EXEMPT · Para 56	Always required ALWAYS REQUIRED · Para 36
📄 LIC MEASUREMENT	FCF + Risk Adjustment SAME AS GMM · No simplification	FCF + Risk Adjustment SAME AS PAA · Para 40
🕒 LIC DISCOUNTING	Required if settlement > 1 year CONDITIONAL · Para 59(b)	Always required ALWAYS REQUIRED · Para 40
🛡️ RISK ADJUSTMENT	Required for LIC only PARTIAL · Not for LRC	Required for both LRC and LIC FULL SCOPE · Para 37
⚠️ ONEROUS TEST	FCF vs LRC carrying amount LESS PRECISE · Para 57	CSM-based — absorbs adverse changes MORE PRECISE · Para 47
📦 DATA REQUIREMENTS	Lower — premium-based inputs LOWER · No actuarial modelling	Higher — granular cashflow modelling HIGHER · Actuarial systems needed



Key Insight: LIC measurement is **identical** under both models (FCF + RA). The real divergence is in LRC complexity, CSM tracking, and data demands — PAA is simpler, but **not straightforward** (Grant Thornton, 2021). PSAK 117 permits both models for Indonesian insurers.

PAA for Indonesian P&C Insurers



Motor Insurance (Asuransi Kendaraan Bermotor)

✓ AUTOMATIC PAA ELIGIBLE

1-year coverage period — automatic PAA eligibility confirmed. Largest P&C line in Indonesia per AAUI data. ITB 2025 study confirms PAA eligibility for motor under normal underwriting scenarios.



Property Insurance (Asuransi Properti)

✓ AUTOMATIC PAA ELIGIBLE

Typically issued on **1-year policy terms**, qualifying automatically for PAA. Simplified LRC measurement applies — no CSM tracking required under PSAK 117.



Travel Insurance

✓ AUTOMATIC PAA ELIGIBLE

Short-duration contracts (days to weeks) — well within the 1-year PAA threshold. Premium-based LRC measurement applies; revenue recognised over coverage period.



Health Insurance (Annually Renewable)

✓ AUTOMATIC PAA ELIGIBLE

Annual renewal structure means each policy year is assessed independently — PAA eligible per contract year. Onerous test still required if facts and circumstances indicate loss.



OJK Regulatory Requirement: Quarterly PSAK 117 reporting mandatory from Q1-2025 — some insurers noted with compliance issues per OJK June 2025 report.

Legal Basis: POJK No. 22/2024 & SEOJK No. 23/SEOJK.05/2024

Numerical Example: Motor Insurance Under PAA

LRC AT INCEPTION

Rp **1,080,000**

Premium 1,200,000 – Acq. Cost 120,000

MONTHLY REVENUE

Rp **90,000**

Straight-line over 12 months

LRC AT Q2 (30 JUN)

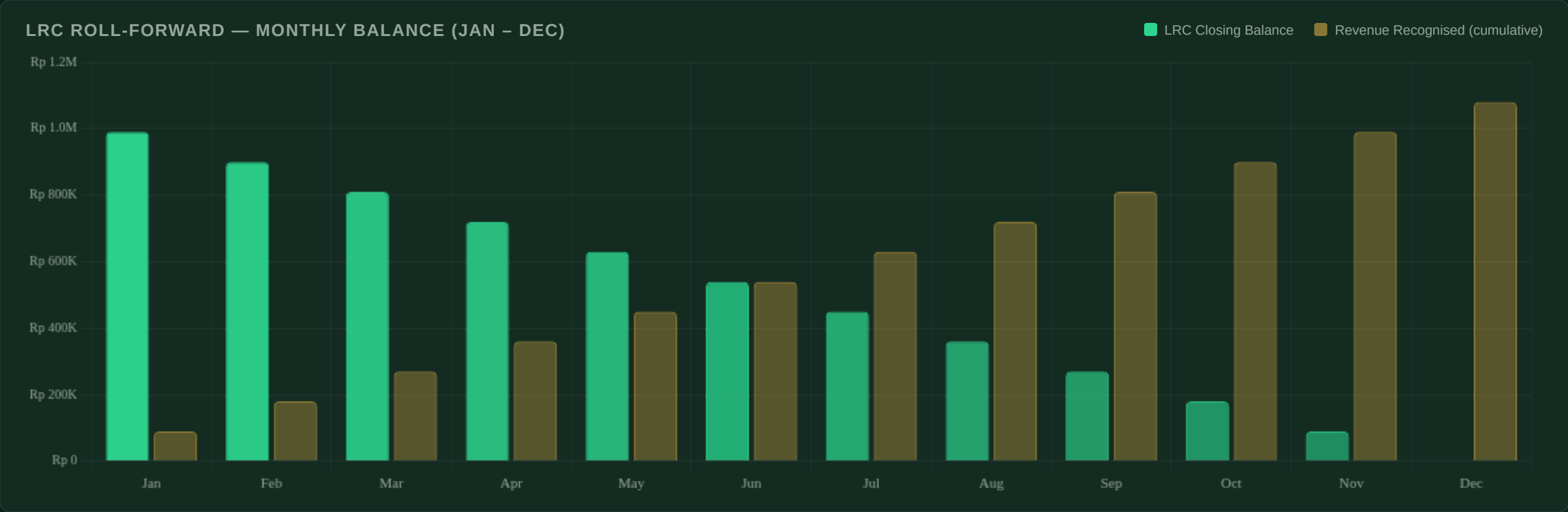
Rp **540,000**

Q1: 810,000 · Q3: 270,000

LRC AT YEAR-END

Rp **0**

All revenue fully recognised



⚠ LIC (Liability for Incurred Claims): If a claim of **Rp 800,000** is incurred in March → LIC = Best Estimate of FCF + Risk Adjustment (RA). Settled within 12 months → **no discounting required** (IFRS 17 Para 59 / PSAK 117). LIC is measured on GMM principles regardless of PAA simplification on LRC.

Key Takeaways & What's Next

EPISODE 5 · PAA RECAP



TAKEAWAY 1

PAA Eligibility

Contracts **≤1 year** qualify automatically. Contracts **>1 year** require a materiality test — demonstrating PAA results are not materially different from GMM.



TAKEAWAY 2

LRC: Simplified Measurement

LRC uses a **UPR-like premium-based** calculation. No PVFCF, no Risk Adjustment, and no CSM tracking required — significantly reducing actuarial complexity.



TAKEAWAY 3

LIC: Still GMM Principles

LIC is **not simplified** — still requires current **FCF estimates + Risk Adjustment**. Discounting applies if claim settlement exceeds 12 months (Para 59).



TAKEAWAY 4

Onerous Contracts: Test Still Mandatory

PAA does not exempt onerous testing. If **FCF > LRC**, a Loss Component is recognised immediately in P&L — checked at every reporting date under PSAK 117.



COMING NEXT · EPISODE 6

Liability for Incurred Claims (LIC)

Deep-dive into **IBNR estimation**, claims development triangles, and **discounting mechanics** under IFRS 17 — with practical examples for Indonesian P&C insurers.

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References & Sources

EPISODE 5 · PAA

All sources cited throughout *IFRS 17 Explained — Episode 5: Premium Allocation Approach (PAA) under IFRS 17 & PSAK 117*.

OFFICIAL STANDARDS & ACADEMIC

OFFICIAL STANDARD

IFRS 17 — Para 53–59, 32–52, 47–52

PAA measurement (Para 53–59), GMM/BBA framework (Para 32–52), Loss Component recognition (Para 47–52). IASB, effective 1 January 2023.

INDONESIAN STANDARD

PSAK 117 — IAI / OJK

Indonesian adoption of IFRS 17. Primary measurement model for general (P&C) insurers in Indonesia, including PAA eligibility criteria.

REGULATION

POJK No. 22/2024 & SEOJK No. 23/SEOJK.05/2024

OJK implementing regulations for PSAK 117 adoption by Indonesian insurance entities. Transition and disclosure requirements.

ACADEMIC · 2025

ITB / Aprilia Dianpermatasari (2025)

PAA eligibility study for motor insurance contracts under PSAK 117. Institut Teknologi Bandung actuarial research.

PRACTITIONER & INDUSTRY

PRACTITIONER · 2021

Grant Thornton (2021)

Is the PAA Really Any Simpler Than the GMM? Comparative analysis of PAA vs GMM complexity, eligibility testing, and operational impact for insurers.

PRACTITIONER · 2025

LinkedIn / Madhurr Vinay Jain (2025)

Premium Allocation Approach — IFRS 17. Practitioner commentary on PAA mechanics, LRC roll-forward, and LIC measurement under IFRS 17.

ACTUARIAL · MAY 2023

CIA / CAS (May 2023)

IFRS 17 Discount Rates and Cash Flow Considerations for P&C. Canadian Institute of Actuaries & Casualty Actuarial Society joint guidance paper.

INDUSTRY DATA

AAUI — Asosiasi Asuransi Umum Indonesia

Indonesia general insurance industry statistics. Motor insurance premium benchmarks (Rp 1–3 million/year) and acquisition cost norms (8–12% of premium).

Source Coverage: Sources span official IASB/OJK standards, Indonesian actuarial research (ITB 2025), global practitioner guidance (Grant Thornton, CIA/CAS), and domestic industry data (AAUI) — ensuring regulatory, academic, and market perspectives.